3 Robert Street
London
WC2N 6RL

Telephone: 020 7543 5600
Facsimile: 020 7543 5700
www.cipfa.org.uk

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Stephenie Fox
Technical Director
International Public Sector Accounting Standards Board
International Federation of Accountants
277 Wellington Street, 4th Floor
Toronto, Ontario M5V 3H2
CANADA

2 April 2009

Dear Stephenie Fox

Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities:

- **The objectives of financial reporting**
- **The scope of financial reporting**
- **The qualitative characteristics of information included in general purpose financial reports**
- **The reporting entity**

1 We are pleased to be able to present comments on this IPSASB Consultation Paper. The development of this response has been co-ordinated by CIPFA, seeking to bring together a range of views from the United Kingdom, including other UK accountancy bodies, public sector practitioners, and other stakeholders in public sector financial reporting. A list of those who provided their views is provided at Annex A.

2 Those listed at Annex A have considerable experience of commenting on financial reporting over several decades, including more recent consultations on conceptual framework related projects such as

- the UK Statement of Principles for Financial Reporting
- the Interpretation for Public Benefit Entities, which extended that framework to cover public benefit entities
- the IASB Conceptual Framework project Discussion Papers and Exposure Drafts, and other IASB related consultations with a significant conceptual element such as the Canadian Accounting Standards Board discussion paper on measurement
- IPSASB consultations with a significant conceptual element, such as the recent consultation paper on Social Benefits

General Comments

3 A sound conceptual framework is vital to the development of principles based financial reporting standards, regardless of sector, and we would see benefits in a sector neutral framework which covered profit-seeking enterprises, public sector

bodies and wider public benefit entities. However, while international standards are increasingly being adopted in all economic sectors, a single conceptual framework underpinning a single set of financial reporting standards is not a realistic expectation at present.

4 We therefore welcome the work which the IPSASB is carrying out on developing a conceptual framework for public sector financial reporting. This is very helpful when there are concerns that developments in the IASB framework may have the effect of making it more difficult to adapt or interpret International Financial Reporting Standards (IFRS) for a public sector context. This important work is timely, and may lead to significant improvements in public sector financial reporting.

5 We are also very supportive of IPSASB's project to develop a suite of IFRS converged IPSASs on relevant issues, using an approach which, in addition to making helpful terminological changes and refocusing examples, might be seen as interpreting the relevant IAS or IFRS as if had been prepared under an overarching framework applicable to all economic sectors.

6 Against this background we agree with IPSASB that the public sector Framework should not simply *interpret* the IASB framework. However we would also note that there are very substantial advantages to maintaining alignment with the IASB framework where this is possible and appropriate. Comparable financial reporting can be expected to have benefits arising from

- better comparability and mutual intelligibility between economic sectors which transact trillions of dollars of business with each other
- skills transfer between public and private sector
- transfer of good practice between sectors

7 We therefore support the inclusion in this paper of the Comparison of IPSASB Preliminary Views with Current IASB Proposals/Preliminary Views (Attachment 1). The consultation paper also notes that concepts underlying statistical financial reporting will be considered in developing the IPSASB Framework, and that the Board is committed to minimizing divergence from statistical financial reporting models. We suggest that the eventual Exposure Draft of the IPSASB framework should include a comparison with relevant aspects of statistical financial reporting models.

8 We also agree that the primary focus of the IPSASB Conceptual Framework should be on public sector entities which operate, at least in part, for the benefit of the public. We would note that some public sector entities operating mainly for public benefit may need to include Government Business Enterprises in their consolidated financial statements.

Scope of the Framework

9 The Framework sets out a potentially very broad scope, covering matters which go significantly beyond the current focus on financial statements.

10 We welcome the paper's reassurance that financial statements should remain at the core of financial reporting. However, contributors to this response expressed

a variety of concerns arising from the proposals to broaden the Framework, with two main themes:

- The paper may not be sufficiently clear in setting out the current proposed scope of the Framework, and this makes it difficult to evaluate related material in other Chapters
- Several UK stakeholders have significant concerns over the broader application of conceptual work mainly developed in the context of financial statements (for example, Qualitative Characteristics)

11 We note that Chapter 3 explains that the broadening of the scope will not necessarily be reflected in IPSASs on all matters within that scope, and this provides some reassurance that the Board will exercise caution in carrying out development work on broader scope matters. However, in the light of the concerns noted above, we suggest that the Framework either needs to be developed in stages, or the Board needs to provide greater clarity over the applicability of individual concepts to GPFS and GPFR information respectively.

Other Matters

12 Comments on other Preliminary Views are set out in Annex B. Key points from these include

The Users of GFPRs

We support consideration of wide categories of users, but suggest that it might be helpful for standard setting purposes to assign some priority to the resource provider perspective. When considering the use of limited resources, the resource provider perspective will provide a helpful focus even to citizens who are not taxpayers and who have not provided resources in other ways.

We also suggest that the reference to “special interest groups” is unnecessary, and might result in undue emphasis being accorded to the needs of these users.

The Objectives of Financial Reporting

We strongly support the inclusion of an accountability objective. Accountability has a special status within public sector reporting generally and financial reporting in particular, and it would be helpful if this were further emphasized in the explanatory material which accompanies the Preliminary View. A variety of views were expressed on the relative importance which should be attached to the two objectives within the Preliminary View, which are detailed in Annex B.

13 I hope these comments are helpful contributions to the development of the conceptual framework.

Steven Cain
Policy and Technical Directorate, CIPFA
Tel +44 (0)20 7543 5794
steven.cain@cipfa.org

ANNEX A

Consultation with and Contributions from UK Stakeholders in Public Sector Financial Reporting

Comments from the following have been incorporated into this response.

Accounting Standards Board (ASB)

Chartered Institute of Management Accountants (CIMA)

Chartered Institute of Public Finance and Accountancy (CIPFA)

Financial Reporting Advisory Board (FRAB)

Institute of Chartered Accountants in England and Wales (ICAEW)

Institute of Chartered Accountants of Scotland (ICAS)

Local Authority (Scotland) Accounts Advisory Committee (LASAAC)

National Audit Office (NAO)

Wales Audit Office (WAO)

Richard Laughlin, Professor of Accounting at Kings College London

A draft response to the IPSASB Conceptual Framework Group 1 paper was drawn to the attention of IFAC member bodies based in the United Kingdom and other key UK stakeholders in public sector financial reporting. This and other explanatory material was also published and made available for comment on the CIPFA website.

Some of the contributors listed above have written separately to IPSASB, to provide responses which highlight their distinctive views, which may differ in emphasis and detail from the combined response. Professor Laughlin has also provided an article developing his ideas on the objectives of public sector financial reporting (published in Public Money and Management Volume 28, No 4, August 2008)

RESPONSE TO MATTERS RAISED IN THE REQUEST FOR COMMENT

IPSASB Preliminary View 1 - The Authority of the IPSASB Framework

The IPSASB Framework will not establish new authoritative requirements for financial reporting by public sector entities that adopt IPSASs, nor will it override the Requirements of existing IPSASs.

In selecting accounting policies to deal with circumstances not dealt with in IPSASs or other guidance issued by the IPSASB, public sector entities will refer to, and consider the applicability of, the definitions, recognition criteria, measurement principles, and other concepts identified in the IPSASB Framework.

We agree. The Framework should not override the requirements of standards which have already been issued, but should be the starting point for interpretation or development of financial reporting in circumstances not dealt with in IPSASs.

The Framework will also inform consideration of which IPSAS standards are most in need of updating or revision, and will inform the development of exposure drafts with amended or new requirements.

We note that the Board has developed Guidelines for Modifying IASB Documents, and that in that document, consistency with the developing IPSASB framework is first in the list of contextual factors which inform consideration of whether IPSASB pronouncements should include departures from IASB standards requirements. We suggest that the Framework should include a clear statement that it will also be the starting point for development of any IPSASs on public sector issues which might not be based on IASB standards.

RESPONSE TO MATTERS RAISED IN THE REQUEST FOR COMMENT

IPSASB Preliminary View 2 - General Purpose Financial Reports (GPFRs)

GPFRs are financial reports intended to meet the common information needs of a potentially wide range of users who are unable to demand the preparation of financial reports tailored to meet their specific information needs.

We agree that general purpose financial reporting as defined in Preliminary View 2 provides an appropriate and helpful focus for the IPSASB Framework, and the standards and guidance that may be developed using the Framework.

The distinction made between general purpose financial reporting and special purpose financial reporting is consistent with that used by the IASB in their framework, and in the standards developed by the International Auditing and Assurance Standards Board (IAASB) in their discussion of reporting frameworks under financial statements and other reporting might be carried out, and be subject to audit under International Standards on Auditing (ISAs)

Most of the potential ‘customers’ for IPSASs and other pronouncements will be governments who may be in a position to demand that specific reports are produced, but choose to develop or use general purpose reporting to meet the information needs of a wider range of users.

In many jurisdictions including the United Kingdom, a key role of public sector financial reporting is that it provides a basis for reporting of financial ‘performance’ against legally authorized budgets. We consider that it would be helpful if the explanatory material in the IPSASB Conceptual Framework could refer to this important aspect of public sector financial reporting, although we do not suggest that it should be highlighted in the preliminary view. We recognize that the budgetary reporting currently carried out by governments may constitute general purpose or special purpose financial reporting, or a mixture of both.

RESPONSE TO MATTERS RAISED IN THE REQUEST FOR COMMENT

IPSASB Preliminary View 3 - The Users of GPFRs

As a mechanism for focusing on their common information needs, the potential users of GPFRs of public sector entities are identified as:

- recipients of services or their representatives;
- providers of resources or their representatives; and
- other parties, including special interest groups and their representatives.

The legislature is a major user of GPFRs. It acts in the interest of members of the community, whether as recipients of services, providers of resources, or citizens with an interest in, or need for, particular services or activities.

We broadly agree with the discussion of users in Chapter 2 of this IPSASB Consultation Paper, but we have some detailed comments on the groups identified in the Preliminary View.

UK stakeholders have considered this matter in successive UK consultations on the ASB Statement of Principles: Interpretation for Public Benefit Entities. In line with 2.4(a) of the IPSASB paper, the ASB identified 'present and potential funders and financial supporters' as the primary user group, suggesting that information which was useful to this grouping would also serve then needs of other users. UK respondents to that consultation generally agreed that 'funders and financial supporters' was a good starting point, but that consideration should also be given to the needs of other stakeholders including service recipients.

In reviewing this matter again for this consultation, comments included the following

- the inclusion of 'service recipients' and 'other parties' within potential users helpfully bring into consideration the needs of these other stakeholders

- the description of users does not refer to 'citizens' as an overarching stakeholder category. While it is clear from the supporting material that 'service recipients' is intended to encompass all citizens, it might be helpful if this were more clearly signposted in the Preliminary View.

- it would be helpful if the Preliminary View put more emphasis on the resource provider perspective, as this will often provide a useful focus for the needs of all users.

- The reference to 'special interest groups' may have the effect of putting too much emphasis on these users, whose needs are already served inasmuch as they represent service recipients, resource providers or both of these

It was also agreed that the legislature was a major user of general purpose financial reporting, notwithstanding the fact that they may also be in a position to request specific information.

RESPONSE TO MATTERS RAISED IN THE REQUEST FOR COMMENT

IPSASB Preliminary View 4 - The Objectives of Financial Reporting

The objectives of financial reporting by public sector entities are to provide information about the reporting entity useful to users of GPFRs for:

- accountability purposes; and

- for making resource allocation, political and social decisions.

We strongly agree that the Framework objectives need to reflect on the usefulness of information for both accountability purposes and decision making.

Using the term "accountability" helpfully draws attention to the requirement to report on the stewardship of public resources. It may also be helpful to use a different term to stewardship to signal the special character of public sector reporting in this regard.

'Decision usefulness' is also essential, and in many contexts it overlaps with and complements the accountability objective.

Some UK contributors stressed the relatedness of the two objectives; inasmuch as accountability is characterized in terms of historical information, and decision-usefulness reflects on future prospects

- consideration of future prospects is substantially embedded in the assessment of the historical position at the end of a financial reporting period

- in practice, information on future prospects is mainly informed by past events

Other UK contributors took a contrasting position, suggesting that the main objective of financial reporting is accountability or stewardship, and that decision-usefulness (except inasmuch as it supported accountability) was less important.

One UK contributor suggested that Preliminary View 4 has the effect of presenting accountability and decision-usefulness as sub-components of a single objective, and that it would be better if they were more clearly presented as separate objectives.

Inasmuch as there is a clear and agreed UK view, it is that the objectives proposed by IPSASB distinguish between accountability and decision-usefulness, and this avoids some of the very significant concerns expressed in relation to the 2006 IASB Discussion Paper, which set out a single resource allocation decision-usefulness objective.

RESPONSE TO MATTERS RAISED IN THE REQUEST FOR COMMENT

IPSASB Preliminary View 5 - The Scope of Financial Reporting

The scope of financial reporting encompasses the provision of financial and non-financial information about:

• economic resources of the reporting entity at the reporting date and claims to those resources;
• the effect of transactions, other events, and activities that change the economic resources of the reporting entity and claims to those resources during the reporting period, including cash inflows and outflows and financial performance;
• the reporting entity's compliance with relevant legislation or regulation and legally adopted or approved budgets used to justify the raising of monies from taxpayers and ratepayers;
• the reporting entity's achievement of its service delivery objectives; and
• prospective financial and other information about the reporting entity's future service delivery activities and objectives, and the resources necessary to support those activities.

It also encompasses explanatory material about: (a) the major factors underlying the financial performance of the entity, the achievement of its service delivery and other objectives and the factors which are likely to influence its performance in the future; and (b) the assumptions underlying and major uncertainties affecting the information included in GPFRs.

As noted in the covering letter, all UK contributors to this response expressed reservations about the proposed broad scope, or suggested that clarification or restriction of the scope would be needed.

Comments and suggestions included

- that the Framework should be initially restricted to financial statements, and extended to wider forms of reporting after further development
- that the potentially different verifiability characteristics of 'broader scope' information raised audit and assurance issues
- requests for more clarity on the nature of prospective information which might be attached to financial statements.

Several respondents also expressed very similar concerns to the IASB, when responding to its proposals to extend the scope of the IASB framework from financial statements to financial reporting without further clarification or discussion.

Having made these observations, we agree that all of the matters set out in the Preliminary View are legitimate matters for public sector reporting and are related to financial reporting. There are several areas in which there may be scope for IPSASB to play a constructive role through the development of standardized approaches to including such material in general purpose financial reports.

RESPONSE TO MATTERS RAISED IN THE REQUEST FOR COMMENT

In going beyond the framework for financial statements, we suggest that there may also be a need to develop or use other forms of authoritative pronouncement, including non-mandatory guidance and educational material, or standards which allow for a great deal of flexibility and tailoring to the circumstances of the reporting entity.

Based on these UK views, we suggest that the Board should adopt one of two approaches going forward:

- The development of the Framework could be carried out in (at least) two stages, with initial development mainly focusing on financial statements. This would have the advantage of keeping to a more well-established and better understood body of discussion and theory from which to develop a public sector framework. Under this approach the IPSASB would need to consider how conceptual issues for 'broader scope' projects such as Long-Term Fiscal Sustainability Reporting should be addressed.

- Alternatively the Framework might develop using a broader scope, but with greater clarity over the applicability of individual concepts to GPFS and GPFR information respectively, and might for example parallel the IASB framework proposals. This would have the advantage of maintaining alignment with the IASB framework, but as noted in the comments on Preliminary View 7, we would have some concerns over the applicability of the Qualitative Characteristics. IPSASB might need subsequently to redeliberate this aspect of the Framework taking account of issues arising from future IASB work on management commentary.

IPSASB Preliminary View 6 - Evolution of the Scope of Financial Reporting

The scope of financial reporting should evolve in response to users' information needs, consistent with the objectives of financial reporting.

We agree that the scope of financial reporting should evolve in response to user need.

RESPONSE TO MATTERS RAISED IN THE REQUEST FOR COMMENT

IPSASB Preliminary View 7 - The Qualitative Characteristics of Information Included in GPFRs

The qualitative characteristics of information included in GPFRs of public sector entities are:

- relevance, which encompasses confirmatory value, predictive value, or both;
- faithful representation, which is attained when depiction of economic or other phenomena is complete, neutral, and free from material error;
- understandability;
- timeliness;
- comparability; and
- verifiability (including supportability).

Constraints on financial reporting are materiality, cost, and the balance between the qualitative characteristics.

The proposed qualitative characteristics are similar, but not identical, to those articulated in recent proposals for the IASB Conceptual Framework, on which several of the bodies at Annex A provided formal responses.

Key concerns articulated in response to the IASB consultations were that

- it is unlikely that qualitative characteristics which are appropriate for financial statements are equally appropriate for the wider categories of information envisaged by the IASB framework. The ASB commented specifically on the problems encountered by the standard setter teams which developed the IASB Discussion Paper on Management Commentary.

- the replacement of the qualitative characteristic of “reliability” with “faithful representation” raises problems in the context of financial statements

We suggest the first of these points may cause difficulties in applying the proposed IPSASB Framework. This will need to be addressed through applying one of the approaches discussed in the response to Preliminary View 5. Regardless of whether broader financial reporting remains within the scope of the Framework, further consideration of qualitative characteristics may be required in connection with broader scope projects such as Long Term Financial Sustainability Reporting.

On the second point, we acknowledge that the IPSASB is seeking to maintain alignment with the IASB framework as articulated in the 2008 Exposure Draft, and in this case we agree that the advantages of alignment are greater than the improvements that would be secured by IPSASB using “reliability”.

In addition, we suggest that the Framework should provide additional emphasis on the significance of materiality based on the “context and nature” of financial reporting. This is a significant aspect of the accountability discussion in the United Kingdom, and we expect it will be a common and significant feature in other jurisdictions.

RESPONSE TO MATTERS RAISED IN THE REQUEST FOR COMMENT

IPSASB Preliminary View 8 – Characteristics of a Reporting Entity

The key characteristic of a reporting entity is the existence of users who are dependant on GPFRs of the entity for information for accountability purposes, and for making resource allocation, political, and social decisions.

A public sector reporting entity may be an entity with a separate legal identity or other organizational structure or arrangement.

We agree with the above analysis. It provides sufficient flexibility to accommodate the many approaches which governments may use to organize their activities, and which in some cases may reflect functional or organizational boundaries specifically designed to support accountability to government and other stakeholders (as described in Preliminary View 3), and to inform funding and other decisions.

IPSASB Preliminary View 9 – The Composition of a Group Reporting Entity

A group reporting entity will comprise the government (or other public sector entity) and other entities when the government (or other public sector entity):

• has the power to govern the strategic financing and operating policies of the other entities (a "power criterion"); and

• can benefit from the activities of the other entities, or is exposed to a financial burden that can arise as a result of the operations or actions of those entities; and can use its power to increase, maintain, or protect the amount of those benefits, or maintain, reduce, or otherwise influence the financial burden that may arise as a result of the operations or actions of those entities (a "benefit or financial burden/loss" criterion).

We agree that this is a sensible approach on the basis of which to develop guidance for group entities, although we would note that some jurisdictions will require financial reports to be produced for group entities on a basis more akin to that set out in Preliminary View 8, to support accountability and decision making.

Considering the specific matter of whole of government entities, we accept that the control based approach is more applicable, although again, some flexibility may be required in practice. For example, based on a review of the discussion in Chapter 9, UK commentators from Scotland and Wales suggested that the power and benefit criteria would not provide a basis for the inclusion of Scottish and Welsh entity information within Whole of Government Accounts which the UK government plans to publish. For some whole of government groups it may be necessary to consider other principles based approaches to providing coherent reporting on economic substance.

A Conceptual Framework for Accounting for Public-Benefit Entities

Richard Laughlin

There is a renewed impetus in the International Accounting Standards Board (IASB) and the International Public Sector Accounting Standards Board (IPSASB) to develop a conceptual framework for financial reporting for both private sector and public-benefit entities. This article takes stock of some of the key issues related to this endeavour with particular emphasis on what the objectives should be and whether it is possible to have one conceptual framework for all entities.

Richard Laughlin is Professor of Accounting in the Department of Management, King's College London, University of London.

The search for a conceptual framework for accounting for public-benefit entities (PBEs[1]) in the UK has had reasonably extensive attention, but a number of developments are occurring internationally that are likely to have a considerable impact on the work that has been undertaken to date. The current conceptual framework in the UK is contained in the Statement of Principles (ASB, 1999) and the interpretation and development of this in the specific context of PBEs (ASB, 2007). However, there is a renewed urgency within the IASB and the US Financial Accounting Standards Board (FASB) to develop a new and more far-reaching conceptual framework over the next few years. The IASB have issued a Discussion Paper (IASB, 2006) and an Exposure Draft (IASB, 2008) exploring the objectives and qualitative characteristics of this conceptual framework. Similar ambitious plans are underway in the increasingly influential IPSASB. IPSASB has started work on its own conceptual framework for PBEs, which, as its *Strategy and Operational Plan* makes clear, will 'draw on the work of the IASB framework project particularly since many of the components of that framework are likely to be relevant'. However, as they continue 'the objective of the project is not to simply interpret the IASB framework for the public sector but rather to develop a stand-alone framework using the work of the IASB and other national standard setters as appropriate' (IPSASB, 2007, p. 12). This article takes stock of the renewed interest in developing a conceptual framework, for private sector entities and PBEs, to inform policy debates, particularly in the IPSASB.

The 2006 IASB's 'objectives' discussion paper for General Purpose Financial Reporting (GPFR) (GPFRs in this article include financial statements and narrative reports, such as the operating and financial reviews and corporate governance reports) generated disquiet, even before its publication. In fact the 2006 IASB's discussion paper was accompanied by a minority report disagreeing with the view that a 'stewardship' objective could be subsumed in the preferred 'decision usefulness' objective that the IASB are advocating. This has led to a robust argument in support of this minority view from the Proactive Accounting Activities in Europe (PAAinE)—made up of standard setters across Europe—in partnership with the European Financial Reporting Advisory Group (EFRAG) that stewardship accounting should be a separate objective in any conceptual framework (EFRAG, 2007). (Note: the PAAinE/EFRAG partnership will be referred to as simply EFRAG in this article.)

This article explores the nature and ramifications of this disagreement.

What Should the Objectives Be?

According to the IASB's discussion paper, the objectives of GPFRs 'for business entities[2]…is to provide information that is useful to present and potential investors and creditors and others making investment, credit, and similar resource allocation decisions' (IASB, 2006, OB2). The stated assumption is that this 'decision-usefulness' objective, with its current and future cash flow focus, *includes* a concern with 'providing information useful in assessing management's stewardship' (IASB, 2006, OB28). The IASB's current view is that the objective is 'to provide financial information about the reporting entity that is useful to present and potential investors and creditors in making decisions in their capacity as capital providers' and that GPFRs 'should communicate information about an entity's economic resources, claims on those resources and the transactions and other events and circumstances that change them' (IASB, 2008, S2). In other words, there was and is no need for two objectives.

The argument for two rather than one objective has gained momentum in Europe. This challenge has been driven by policy and theoretical arguments (see Lennard, 2007) and also by an analysis of the comment letters to the discussion paper. The latter leads to the conclusion that '78 per cent of respondents who referred to stewardship/accountability as an issue were of the view that it should be a separate objective in the converged framework' (EFRAG, 2007, p. 3). IASB, it seems, are unconvinced by EFRAG's analysis.

IPSASB seems to have a more open mind on the issue, and actually sees the debate as secondary to a wider purpose, judging by the draft consultation paper which they considered at their March 2008 meeting: 'It can be argued that whether the objective of financial reporting in the public sector is identified as the provision of information for accountability purposes or for decision-making purposes or for both accountability and decision-making purposes is secondary to the identification of the user information needs that GPFRs will respond to' (IPSASB, 2008, 3.65). Interestingly, the IPSASB refer to 'accountability' rather than 'stewardship', maintaining that there 'is a strong case for using accountability to encompass stewardship in the framework' (IPSASB, 2008, 3.74).

A New Way to Explore the Disagreement

Figure 1, which is built around three axes/continuums, provides an analytical framework for exploring this disagreement on objectives.

The horizontal axis makes a key distinction between 'entity accountability' (rather than 'stewardship') and 'decision-usefulness' information. The fundamental difference between these two purposes is well captured by explicating the distinction between what has been called the difference between 'entity' versus 'proprietorship' accounting theory (Mattessich, 1964, p. 37). This distinction, while dated, captures something of lasting importance of which we have too easily lost sight. Entity accounting, or 'entity accountability' as used in this article, is a report about the activities and actions of the entity to inform any and all users, but with no particular users in mind. This concentration on entity accountability avoids the IASB's emphasis of making sure that the GPFRs meet the information needs of 'primary users' (IASB, 2008, S2). Proprietorship accounting, or decision-usefulness information, is concerned with reports for particular stakeholders for particular purposes and can be seen as a separate objective even if the concentration is only on GPFRs. The centre of the horizontal axis is the cross-over point between entity accountability and decision-usefulness. Where any information straddles this point then it is likely to be relevant for *both* entity accountability and decision-usefulness purposes.

The vertical axis highlights that there can be increasing *levels* of entity accountability and decision-usefulness information. Closer to the base on either continuum, the information is not as comprehensive entity accountability or decision-usefulness information as would be the case nearer the top of these continuums. The assumption is that being positioned at the top of either continuum would include everything below. This is certainly the case in terms of entity accountability. This is not as clear-cut, however, when it comes to decision-usefulness information, since this can range from GPFRs at the lower levels (which have implicit user needs in mind, despite their apparent general nature), to more explicit reports for specific users for specific purposes at the highest point. The latter might only partially refer to the former and, in certain circumstances, may make no reference to it at all.

This distinction is reflected in the diagonal, sloping axis in the body of the figure. This axis highlights a distinction between the different structural nature of the resulting reports, ranging from GPFRs for all users, to specific reports for different users for different decision-usefulness needs. What is also apparent from figure 1 is that some GPFRs have particular users and particular decision-usefulness information needs clearly in mind. This becomes more apparent when these reports are positioned further away from the mid-point on the horizontal axis and higher up the vertical axis, on the decision-usefulness side.

Figure 1 provides a different way of exploring the disagreement between the IASB's and EFRAG's understanding of stewardship and decision-usefulness—with the latter depicted as a 'cash flow focus', due to this being the dominant emphasis of the IASB's understanding of decision-usefulness information. Despite the strident disagreement, figure 1 shows that there is not as much distance between the two as the debates would seem to

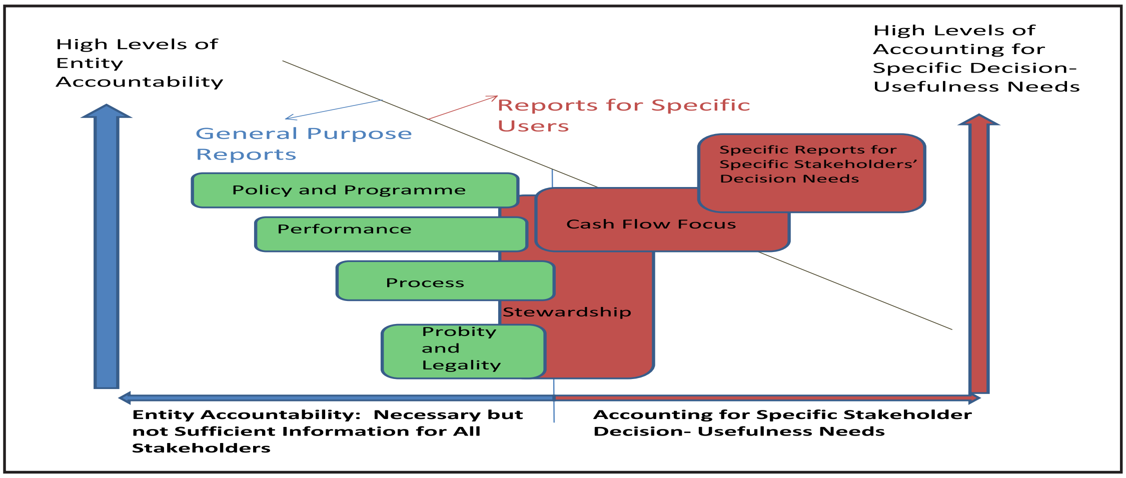

Figure 1. Conceptualizing entity accountability and decision-usefulness.

suggest. Stewardship reporting sits on the borderline between entity accountability and decision-usefulness information. Yet, as EFRAG (2007) make clear, the commonly-accepted understanding of stewardship, based on both their view as well as those who responded to the discussion paper, has an underlying decision-usefulness emphasis. This is summarised well when EFRAG highlighted that 'most respondents that commented on stewardship consider that the stewardship objective is about assessing management's competence and integrity including the success of their strategy in managing the business. They state that one objective of financial reporting should be to serve as a type of dialogue between management and shareholders with the information they need to make decisions, as owners of the business' (EFRAG, 2007, p. 6). Given this understanding, the IASB, not surprisingly, are of the view that this stewardship objective can be achieved within their wider decision-usefulness objective. This is rather belittling of the differences but, at another level, it is possible to make this claim. To reinforce this point it is worth noting the view of one of the respondents to the IASB's discussion paper, echoing the view of the IASB, when they made clear: 'we believe that the concept of stewardship is embodied in and is an essential part of decision-usefulness information' (EFRAG, 2007, p. 8).

Stewardship reporting, as understood by EFRAG, has a 'weak' decision-usefulness emphasis relative of the 'strong' emphasis of the IASB and the FASB. The two objectives share a common decision-usefulness 'worldview' making them 'not fully alternatives at all, but simply adjustments within the user worldview.....even though this commonality is not necessarily evident to the proponents' (Laughlin and Puxty, 1983, p. 475).

What figure 1 also highlights is that the IASB's suggested 'cash flow focus' is only partly satisfying the decision-usefulness objective they are proposing. While the 'cash flow focus' of the IASB is still a GPFR its emphasis is geared to the specific needs of finance-providers—hence it is positioned both to the right hand side of figure 1, as well as crossing over the diagonal axis. It is, however, higher up the decision-usefulness vertical axis. But what figure 1 also makes clear is that if the decision-usefulness objective is to be fully achieved, then there needs to be a move to the top far right of figure 1. This involves developing specific reports for specific stakeholders for particular decision needs. Logically, a GPFR report is never going to achieve this. The danger, based on the logic of figure 1, is that the further the GPFR moves away from the left-hand side of the diagram the more these reports fail to satisfy entity accountability.

Entity Accountability: An Explication

More needs to be said about entity accountability and the four different levels depicted in figure 1. One of the key characteristics of entity accountability is that it does not have a 'primary user group' in mind. Accountability can be described as 'the giving and demanding of reasons for conduct' (Roberts and Scapens, 1985, p. 447), but does not necessarily require a specification of who does the 'demanding'. In this regard, entity accountability is not directly concerned with the needs of users but with the entity and its actions and activities both in terms of the past as well as in relation to future intentions. Entity accountability is intended to be useful, at some level, to all stakeholders but there is less concern about either who these stakeholders are or what their information needs may be in any specific sense. It is for this reason, as is apparent from figure 1, the resulting information is deemed to be 'necessary but not sufficient for all stakeholders'.

In addition, entity accountability is what can be described as 'political/public', rather than 'managerial', accountability, since the latter has a stronger decision-usefulness emphasis. Day and Klein (1987, pp. 26–27) highlight the differences between these two forms of accountability in the following way: 'Political accountability is about those with delegated authority being answerable for their actions to the people, whether directly in simple societies or indirectly in complex societies…In contrast, managerial accountability is about making those with delegated authority answerable for carrying out agreed tasks according to agreed criteria of performance'.

Political/public entity accountability can be at four different levels in a 'ladder of accountability' according to Stewart (1984, pp. 17–18). At the base, and the most basic, entity accountability is an account about *probity and legality*. This is primarily an account about the receipt and use of money entrusted to the entity to demonstrate that it satisfies a range of requirements, not least compliance with the law. *Process accountability* provides information on the internal processes through which the entity undertakes its work of converting inputs into outputs and outcomes. *Performance accountability* involves making transparent expected and actual performance related to entity objectives notably in terms of outcomes forthcoming. Finally, *policy and programme accountability*, involves information on broader policy issues that drive the reporting entity and the programmes that it is pursuing over particular timeframes. The four levels are indeed a 'ladder', which assumes that each 'step' builds on the previous 'step' so that, at the top of the ladder, all the steps are articulated to provide a comprehensive understanding of the reporting entity.

The Objectives Question

Figure 1 allows the 'one versus two objectives' argument to be viewed in a different way. If the alternatives are posed in terms of stewardship versus decision-usefulness, as currently understood by EFRAG and the IASB, then the latter is right to say that stewardship can be subsumed in decision-usefulness. However, if the alternatives are between entity accountability and decision-usefulness, then this poses a real choice. But it can be argued that this choice should not have to be made. A not unreasonable view, if accounting is to serve an important societal purpose, is that both entity accountability as well as decision-usefulness information are important and, therefore, the conceptual framework should pursue both objectives.

There is, however, a need to be more adventurous as to how these objectives are implemented in the design of actual accounting statements. Currently both the IASB/FASB and EFRAG continue to advocate GPFRs, albeit differing on the contents of these reports. This has to be a severe limitation, particularly for the IASB and FASB, who wish to pursue *only* a decision-usefulness objective. To be effective in achieving this objective there needs to be a more specialist focus leading to specific reports for specific users for specific decisions. As indicated above, GPFRs rapidly become an irrelevancy under decision-usefulness thinking. However, GPFRs, for those pursuing entity accountability, are never an irrelevancy. The question for the proponents of entity accountability is what should be contained in the GPFRs. In this connection, to stop at the probity and legality level is difficult to justify given the other levels in Stewart's 'ladder of accountability'.

One Conceptual Framework and One General Purpose Entity Accountability Report for All Private Sector Entities and PBEs?

Whether there should be *one* conceptual framework for *all* entities is a question that applies whether or not it is built on two rather than one objective(s). One view on this question is well captured by the Government Accounting Standards Board (GASB) in the USA: 'separate accounting and financial reporting standards are essential because the needs of users of financial reports of governments and business enterprises differ' (GASB, 2006, p. 1). While GASB's economic distinctiveness argument is difficult to refute, their conclusion is more suspect. What they are doing is using decision-usefulness logic in relation to entity accountability. An alternative view is held by the IASB who are content to let the unfortunately named 'not-for profit' sector to be picked up late in the conceptual framework project. The implication of this is that differences between the sectors are so small that the consideration of PBEs can be left until all the other major issues have been resolved. IPSASB clearly does not share this view, as their early endeavours to produce a conceptual framework for PBEs demonstrate, but that does not mean that they agree with the views of the GASB, or the IASB.

Conceptually there should be a *single*

conceptual framework, arguably built on two objectives, for *all* entities, but this doesn't mean that the resulting information will be, or should be, the same across all entities. There are good reasons why entity accountability *and* decision-usefulness information should become the underlying basis of a unified conceptual framework. However, at lower levels in the conceptual framework, dealing with the actual content of the information supplied across the different entities, this could and should differ.

This is most obvious in relation to fulfilling the decision-usefulness objective, given the different stakeholders involved and their different decision needs. This also assumes that to satisfy a decision-usefulness objective cannot realistically be fully achieved by GPFRs, despite the IASB's seeming support for this possibility. However, the IASB, with their 'primary users' in mind and their cash flow emphasis, are stretching GPFRs to the extremes of general relevance as figure 1 highlights.

This conclusion, however, is not so clear-cut in relation to entity accountability. The assumption over many years is that private sector financial reporting and accompanying domestic and international accounting standards, taking aside, for the moment, the narrative reporting requirements, will satisfy some of the accountability needs of PBEs. The validity of this argument is explored below.

Entity Accountability: Conceptualizing Commonalities

One view on this is that this strategy has been incorrect on the grounds that the economic nature of PBEs and private sector entities is fundamentally different. Simpkins (2006, p. 16) summarises these differences by typecasting PBEs as follows:

'• their objective is to provide goods and services to various recipients or to develop or implement policy on behalf of governments and not to make a profit;
• they are always characterized by the absence of defined ownership interests that can be sold, transferred or redeemed;
• they typically have a wide group of stakeholders to consider (including the public at large);
• their revenues are generally derived from taxes or other similar contributions obtained through the exercise of coercive powers;
• and their capital assets are typically acquired and held to deliver services without the intention of earning a return to them'.

A similar listing is contained in GASB's (2006) white paper. It is difficult to dispute the reality of these differences.

While these differences are significant, this still does not necessarily mean that, at a probity and legality level, separate accounting standards are needed for respectively private sector entities and PBEs. This is because there are some economic commonalities across all entities.

Figures 2 and 3 provide a very basic understanding of these economic commonalities in and differences between the two sets of entities. The figures depict private sector entities and PBEs as an amalgam of three subsystems—a decision and control subsystem that both controls the entity as well as receives inputs and outputs information to the entity's environment; a funds subsystem which both receives and spends money; and an operations subsystem which receives non-financial inputs and processes these into outputs and outcomes (cf. Lowe, 1972; Bebbington *et al.*, 2001). The key assumption in both figures 2 and 3 is that there are three generic fundamental financial transactions of any entity from which financial statements are drawn. There are other transactions—notably those related to credit rather than cash exchanges—but these are refinements to the three transactions highlighted in figures 2 and 3 rather than being of a fundamentally different nature.

Transaction 1 is the capitalization funding flow to allow the entity to function. Transaction 2 involves the expenditure by the entity on inputs needed for the long and short term. Transaction 3 is the financing that comes from and links to these outputs and outcomes achieved. As is apparent from both figures, these transactions have an input and output into and out of the entity. In all cases in figure 2 these are closely connected, but this is not the case in figure 3. Recording this duality, notably for private sector entities, is why double entry book-keeping came into being.

Figure 2 portrays these transactions in relation to private sector entities. The funds input in transaction 1 are receipts from ownership claims and from liability holders. These are connected to outputs from the decision and control subsystem, which contains the formal contractual acknowledgement of indebtedness either in terms of ownership recognition or loan arrangements. Transaction 2 involves the purchase of 'factors' for the production of goods and services, whether of a long-term (asset) or more short-term (current) nature. Again, there is a clear connection between the funds output and the input into the operation's subsystem. Transaction 3 involves the receipts from market sales of the outputs generated by the entity. Again, the connection between the input into the funds subsystem and output from the operations subsystem is clear because of the market which prices (and values) the products and services sold.

Figure 3 demonstrates that similar transactions exist in PBEs even though the input/output connections are more complex. Transaction 1 indicates that there are capital receipts in PBEs, but there is a lack of clear linkage between these input receipts and any apparent outputs. In the private sector there is always some acknowledgement of indebtedness—marked as an output from the decision and control subsystem. This is not the case in PBEs. There is a genuine uncertainty in the capitalization arrangements of PBEs as to the nature of their indebtedness and/or in relation to ownership claims. Clearly this does not apply to legal liabilities, which are similar to those taken out in private sector entities. Transaction 2 is exactly the same for both PBEs as well as for private sector entities and the same problems with regard to asset and expense classification applies across all entities. The distinction between asset and expense is highly problematic in accounting in all entities due to the similarity of the input into the operations subsystem. The financial scandals of Worldcom and Parmalat are traceable to this problem of deciding when operations inputs are assets or expenses. Ever since resource accounting and budgeting was introduced into the UK public sector, this has been a common problem for both private sector entities and PBEs.

There are, however, inputs into the operations subsystem that have *not* been purchased through a market exchange. These are marked 'transaction 2A' in figure 3. These inputs include gifts of time, property etc. Yet, while these are similar to transaction 2, there is no obvious output apart from, if they are a gift, some information flow (such as an appreciative acknowledgement) from the decision and control subsystem. Transaction 2A causes immense difficulties as to how to account for these as inputs and outputs. So even in transaction 2 the duplication between private sector entities and PBEs is not without problems for the latter. Yet there are certainly more commonalities in transaction 2 than in transaction 1. Finally, with regard to transaction 3, there is a marked difference between private sector entities and PBEs. The connection between funds received by the PBEs (for example government grants) and the services delivered do not have the clear market linkages that are apparent in private sector entities.

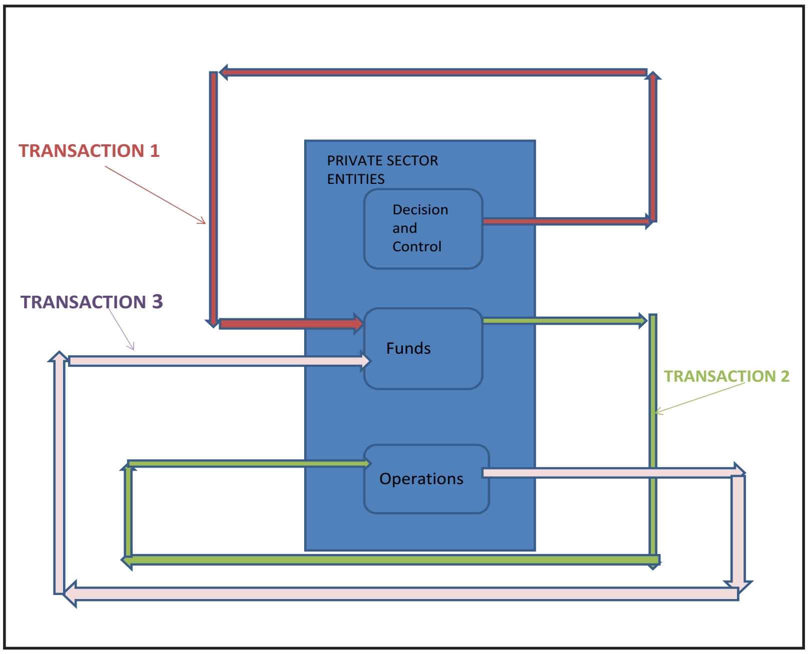

Figure 2. Key transactions in private sector entities.

Entity Accountability: Some Answers

What figure 2 and 3 demonstrate is why private sector financial statements fits better for private sector entities and why some of the underlying concepts and standards need reshaping to allow them to fit the context of PBEs.

There are a number of recent examples that illustrate this. Take, for instance, struggles with the definition of liabilities in the Statement of Principles for PBEs (ASB, 2005a, 2007) and the difficulties related to how best to account for heritage assets (ASB, 2006a, 2006b). Both problems are traceable to the fact that the economic and social nature of private sector entitles and PBEs differ. Liabilities have been resolved by providing a genuine PBE solution. Heritage assets are less straightforward and remain a problem. Heritage assets are mainly found in PBEs. Only some of them are purchased through a market exchange. The original discussion paper (ASB, 2006a) posed a PBE accounting solution, which involved giving either a value to an entire collection if this could be done, or providing a more qualitative description if it couldn't. This 'all or nothing' approach, despite the support received in the consultation, was changed in the Exposure Draft (ASB, 2006b) to, in effect, a private sector solution to a PBE problem by requiring balance sheet valuations, but on individual separate items in collections rather than the collection as a whole. This assumes market values for these individual assets are attainable—something which is unproblematic with private sector assets but is problematic in many cases with heritage assets. Whether this will be the final standard remains to be seen.

In other cases, such as with defining and recording assets (but not for those assets acquired in a different way to a market exchange) and expenses, there have been no such similar problems and struggles. This is because of the commonality of transaction 2, in large measure, across all entities as is apparent from figures 2 and 3.

On balance, therefore, the strategy to use private sector accounting standards for PBEs has been useful and it is appropriate to continue, but this is not without two caveats:

- Private sector standards need to be judged against whether their application distorts the representation of the different nature of the economic reality of PBEs. If this is the case the application needs to be questioned.
- The resulting entity accountability report is only likely to satisfy, at best, the probity and legality level of Stewart's ladder.

In this context a further question is whether entity accountability requirements for PBEs in terms of Stewart's higher levels of accountability, can be satisfied with private sector 'narrative reporting'. Here the answer is again less than absolutely clear. Certainly the Operating and Financial Review (OFR) when it was a 'Reporting Standard' (ASB, 2005b) and even as a 'Reporting Statement' (ASB, 2006c), even though it has a private sector emphasis, has generic qualities making it potentially a basis for developing a PBE version. This has been suggested and analysed by RSM Robson Rhodes and CIPFA (2006a, 2006b). However, with a shift in narrative reporting away from the OFR to the business review in the directors' report in the private sector, the relevance of this development for satisfying higher levels of entity accountability for *both* private sector entities *as well as* PBEs has to be questionable.

This change would suggest that to satisfy higher levels of entity accountability in PBEs would require a rather different set of reports than could be satisfied either by the predominantly private sector OFR or certainly the business review. Interestingly this is also the conclusion of RMS Robson Rhodes and CIPFA (2006b) following their analysis of the OFR for PBEs.

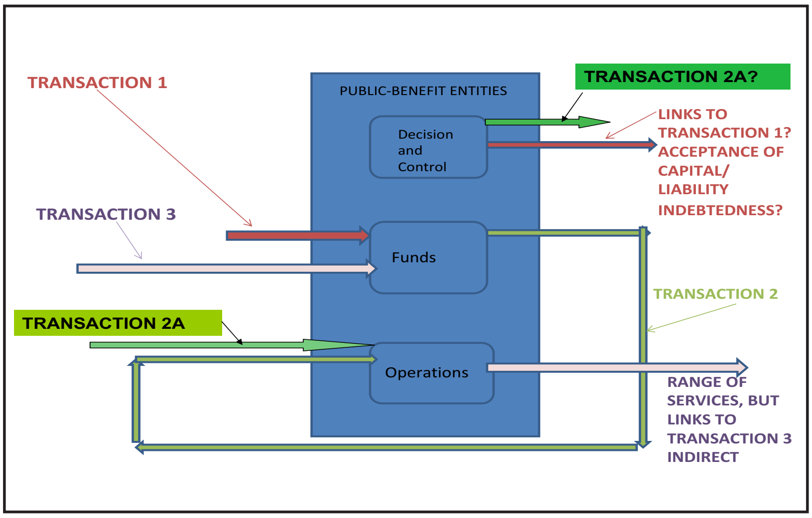

Figure 3. Key transactions in public benefit entities.

Concluding Thoughts

This article raises important, fundamental questions about the objectives of accounting in a conceptual framework. This analysis leads to three pragmatic recommendations. The pragmatism is because history cannot be rewritten and it is impossible to start from a different point than the current situation, no matter how much this might be preferable.

First, it is important to maintain the pressure that the ASB and EFRAG have exerted over the IASB, FASB and IPSASB for having two rather one objective for the conceptual framework for accounting for both private sector entities, as well as PBEs. But there needs to be a change in one of the objectives from stewardship to entity accountability.

Second, probity and legality entity accountability for PBEs should continue to be based on financial accounting standards that apply to private sector entities but, at the same time, recognize that the economic and social nature of these entities is different and, therefore, some private sector standards might not be appropriate for PBEs. What this would involve is less of an unbending application of private sector rules when this would distort the nature of the reality being represented. Liability recognition is a good illustration of how this can be achieved, while the current exposure draft for accounting for heritage assets is not.

Third, there needs to be an expansion of both entity accountability, as well as decision-usefulness information for all entities. In terms of the former this would involve going beyond the adaptation of current private sector financial statements and narrative reporting to more expansive probity, legality, process, performance, policy and programme accountability statements for both private sector entities and PBEs. To achieve this objective would require developing GPFRs in new ways. This needs to be accompanied with a development of specific information for specific decision-making for specific stakeholders in both private sector entities and PBEs. This will involve often once-off information to be supplied, in addition to the new GPFRs. Taking these developments together will lead to a meaningful conceptual framework for both private sector entities as well as PBEs, as well as meaningful information and useful information for all. ■

Notes

[1]'PBEs' are the increasingly common descriptor of public service organizations by policy bodies. PBEs include organizations that are not just those located in the public sector but have a public-benefit concern wherever located. In the academic literature this has given rise to describing this wider set of organizations as 'public services' some of which are part of the 'public sector' (see Broadbent and Guthrie, 2008). However, in this article the descriptor of PBEs is used.

[2]The IASB and FASB do make plain that this objective has a particular business emphasis and that this will be reconsidered when they come to look at what they call 'not-for-profit' organizations at a later stage in the development of their conceptual framework. The assumption is that the objective might need slight modification in specifics but not in its underlying emphasis, no matter which entities are being considered.

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